

ISLAND CITY ACADEMY
REPORT ON FINANCIAL STATEMENTS
(with required supplementary and additional information)
YEAR ENDED JUNE 30, 2007

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INDEPENDENT AUDITORS' REPORT

To the Board of Education
Island City Academy
Eaton Rapids, Michigan

September 21, 2007

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Island City Academy (the Academy), as of and for the year ended June 30, 2007, which collectively comprise the Academy's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Academy's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of Island City Academy as of June 30, 2007 and the respective changes in financial position, thereof, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

To the Board of Education
Island City Academy
Eaton Rapids, Michigan

September 21, 2007

In accordance with *Government Auditing Standards*, we have also issued our report dated September 21, 2007, on our consideration of Island City Academy's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis and budgetary comparison information on pages vi through xi and 20, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Island City Academy's basic financial statements. The additional information on pages 22 and 23 is presented for purposes of additional analysis and is not a required part of the basic financial statements. This additional information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Maner, Costrison & Ellis, P.C.

Certified Public Accountants

MANAGEMENT’S DISCUSSION AND ANALYSIS

This section of Island City Academy’s (the Academy) annual financial report presents our discussion and analysis of the Academy’s financial performance during the fiscal year that ended on June 30, 2007.

FINANCIAL HIGHLIGHTS

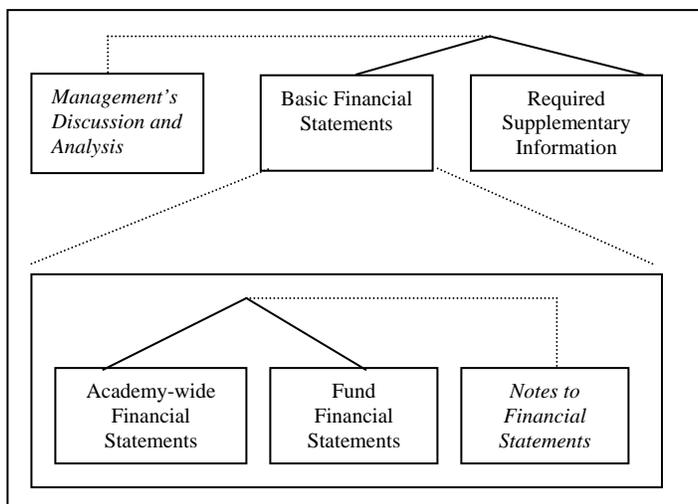
- The Academy’s financial status remained stable for the third year in a row, total net assets increased by approximately \$240,000.
- Overall revenues were approximately \$1,513,000
- The total cost of instruction programs increased approximately \$39,000.
- Total revenues increased approximately \$276,000, while total expenses increased approximately \$163,000.
- Enrollment increased by approximately 20 students from the prior year.
- The Academy reduced its outstanding long-term debt \$30,000.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of three parts - management’s discussion and analysis (this section), the basic financial statements and required supplementary information. The basic financial statements include two kinds of statements that present different views of the Academy:

- The first two statements are *academy-wide financial statements* that provide both *short-term* and *long-term* information about the Academy’s *overall* financial status.
- The remaining statements are *fund financial statements* that focus on *individual parts* of the Academy, reporting the Academy’s operations *in more detail* than the academy-wide statements.
- The *governmental funds* statements tell how *basic* services like regular and special education were financed in the *short-term* as well as what remains for future spending.
- *Fiduciary funds* statements provide information about the financial relationships in which the Academy acts solely as a *trustee or agent* for the benefit of others.

**Figure A-1
Organization of Island City’s
Annual Financial Report**



Summary ← → **Detail**

The financial statements also include *notes* that explain some of the information in the statements and provide more detailed data. The statements are followed by a section of *required supplementary information* that further explains and supports the financial statements with a comparison of the Academy’s budget for the year. Figure A-1 shows how the various parts of this annual report are arranged and related to one another.

Figure A-2 Major Features of Academy-wide and Fund Financial Statements			
	Academy-wide Statements	Fund Financial Statements	
		Governmental Funds	Fiduciary Funds
Scope	Entire district (except fiduciary funds)	The activities of the school that are not proprietary or fiduciary, such as special education and building maintenance.	Instances in which the school administers resources on behalf of someone else, such as scholarship programs and student activities monies
Required financial statements	* Statement of net assets * Statement of activities	* Balance sheet * Statement of revenues, expenditures and changes in fund balances	* Statement of fiduciary net assets * Statement of changes in fiduciary net assets
Accounting basis and measurement focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus
Type of asset/liability information	All assets and liabilities, both financial and capital, short-term and long-term	Generally assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets or long-term liabilities included	All assets and liabilities, both short-term and long-term, Island City's funds do not currently contain capital assets, although they can.
Type of inflow/outflow information	All revenues and expenses during year, regardless of when cash is received or paid	Revenues for which cash is received during or soon after the end of the year, expenditures when goods or services have been received and the related liability is due and payable	All additions and deductions during the year, regardless of when cash is received or paid

Figure A-2 summarizes the major features of the Academy’s financial statements, including the portion of the Academy’s activities they cover and the types of information they contain. The remainder of this overview section of management’s discussion and analysis highlights the structure and contents of each of the statements.

ACADEMY-WIDE STATEMENTS

The academy-wide statements report information about the Academy as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets include *all* of the Academy’s assets and liabilities. All of the current year’s revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two academy-wide statements report the Academy's *net assets* and how they have changed. Net assets - the difference between the Academy's assets and liabilities - are one way to measure the Academy's financial health or *position*.

- Over time, increases or decreases in the Academy's net assets are an indicator of whether its financial position is improving or deteriorating, respectively.
- To assess the overall health of the Academy, you need to consider additional nonfinancial factors such as changes in the Academy's revenue streams and the condition of school buildings and other facilities. Currently the Academy is near capacity student enrollment and any variation from that may reflect negatively on the overall financial health of the Academy.

In the academy-wide financial statements, the Academy's activities:

- Governmental activities - Most of the Academy's basic services are included here, such as regular and special education, administration and operations and maintenance. State formula aid finances most of these activities.

FUND FINANCIAL STATEMENTS

The fund financial statements provide more detailed information about the Academy's *funds*, focusing on its most significant or "major" funds - not the Academy as a whole. Funds are accounting devices the Academy uses to keep track of specific sources of funding and spending on particular programs:

- Some funds are required by State law and by loan covenants.
- The Academy establishes other funds to control and manage money for particular purposes (like repaying its long-term debts) or to show that it is properly using certain revenues.
- The Academy has added a School Lunch Fund and a Capital Projects Fund to properly account for new activities.

The Academy has two kinds of funds:

- Governmental funds - Most of the Academy's basic services are included in governmental funds, which generally focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the Academy's programs. Because this information does not encompass the additional long-term focus of the academy-wide statements, we provide additional information with the governmental funds statements that explain the relationship (or differences) between them.
- Fiduciary funds - The Academy is the trustee, or fiduciary, for assets that belong to others, such as the scholarship fund and the student activities funds. The Academy is responsible for ensuring that the assets reported in these funds are used only for their intended purposes and by those to whom the assets belong. We exclude these activities from the academy-wide financial statements because the Academy cannot use these assets to finance its operations.

FINANCIAL ANALYSIS OF THE ACADEMY AS A WHOLE

Net assets - The Academy's *combined* net assets were larger on June 30, 2007, than they were the year before - increasing by \$237,248.

The Academy's improved financial position is the product of many factors.

Table A-3		
Island City's Net Assets		
	2007	2006
Current and other assets	\$ 841,784	\$ 673,352
Capital assets	1,817,300	1,778,539
Total assets	2,659,084	2,451,891
Long-term debt outstanding	1,605,000	1,635,000
Other liabilities	214,473	214,528
Total liabilities	1,819,473	1,849,528
Net assets:		
Invested in capital assets, net of related debt:	182,300	113,539
Restricted	208,172	206,116
Unrestricted	449,139	282,708
Total net assets	\$ 839,611	\$ 602,363

Table A-4		
Changes in Island City's Net Assets		
	2007	2006
Revenues:		
Charges for services	\$ 11,250	\$ 4,805
Operating grants	48,428	4,805
General revenues:		
State aid - unrestricted	1,427,053	1,219,158
Local sources	40,173	
Other	15,617	13,831
Total revenues	1,542,521	1,237,794
Expenses:		
Instruction	707,852	674,063
Support services	399,510	359,899
Food services	25,482	
Interest on long-term debt	118,719	123,161
Unallocated depreciation	53,711	40,633
Total expenses	1,305,274	1,197,756
Change in net assets	\$ 237,247	\$ 40,038

FINANCIAL ANALYSIS OF THE ACADEMY'S FUNDS

The strong financial performance of the Academy as a whole is reflected in its governmental funds as well. As the Academy completed the year, its governmental funds reported *combined* fund balances of \$706,702; \$167,581 above last year's ending fund balances of \$539,121.

The Academy's general fund had more revenues than expenditures in 2007 by \$115,660. The debt service fund had more revenues than expenses by \$1,150. The capital projects fund - building and site had revenues and transfers in 2007 of \$50,771. Overall, the Academy had an increase in total fund balance.

General Fund Budgetary Highlights

Over the course of the year, the Academy revised the annual operating budget several times. These budget amendments are:

- Changes made in the second and fourth quarters to account for final enrollment counts and changes in assumptions since the original budget was adopted.

While the Academy's final budget for the general fund anticipated that revenues would be lower than expenditures and transfers out by roughly \$9,100, the actual results for the year show approximately a \$116,000 surplus.

- Actual revenues were \$7,241 higher than expected, due largely to higher enrollment.
- The actual expenditures were \$113,745 below budget, due primarily to various expense reduction practices.
- The Academy board transferred \$50,000 to the capital project fund for building repairs and renovation plans to continue to designate funds to this purpose when fiscally responsible.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

By the end of 2007, the Academy had invested \$1,817,300 in a broad range of capital assets, including school building, computer and audiovisual equipment and other school furniture. This amount represents a net increase of \$38,761, from last year. (More detailed information about capital assets can be found in Note 5 to the financial statements.) Total depreciation expense for the year was \$53,711.

Furthermore, the school received from the Parent-Teacher Organization a substantial donation of playground equipment, a capital asset, with a fair value of almost \$38,000 that was included in land improvements.

Table A-5		
Island City's Capital Assets		
<i>(net of depreciation)</i>		
	2007	2006
Land	\$ 96,082	\$ 96,082
Buildings	1,521,129	1,553,060
Computer equipment	34,650	
Land improvements	37,384	
Equipment and furniture	128,055	129,397
Total	\$ 1,817,300	\$ 1,778,539

Long-term Debt

At year-end the Academy had \$1,635,000 in certificates of participation outstanding- a reduction of \$30,000 from last year. (More detailed information about the Academy's long-term liabilities is presented in Note 6 to the financial statements.)

- The Academy continued to pay down its debt, retiring \$30,000.
- No new debt was issued during the year.

FACTORS BEARING ON THE ACADEMY'S FUTURE

At the time these financial statements were prepared and audited, the Academy was aware of three existing circumstances that could significantly affect its financial health in the future:

- The 2007-2008 foundation allowance has not been finalized by the State of Michigan. The foundation allowance represents 99 percent of total Academy revenue.
- A weak state economy could require pro-rating in state aid.
- The ability to maintain or increase pupil enrollment at the Academy.
- The Academy has added a food service program and thus a Food Service Fund was created which required a transfer from the general fund to cover start-up costs. It is expected that this Food Service Fund will not increase the fund balance of the school.

CONTACTING THE ACADEMY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our parents, customers and investors and creditors with a general overview of the Academy's finances and to demonstrate the Academy's accountability for the money it receives. If you have questions about this report or need additional information, contact the Administrator's Office, Island City Academy, 6421 Clinton Trail, Eaton Rapids, MI 48827.

**ISLAND CITY ACADEMY
STATEMENT OF NET ASSETS
JUNE 30, 2007**

ASSETS	Governmental activities
CURRENT ASSETS:	
Cash	\$ 318,269
Investments	229,219
Receivables:	
Other governmental units	257,995
Prepaid expenditures	36,301
TOTAL CURRENT ASSETS	841,784
NONCURRENT ASSETS:	
Capital assets	2,164,751
Less accumulated depreciation	(347,451)
TOTAL NONCURRENT ASSETS	1,817,300
TOTAL ASSETS	\$ 2,659,084
LIABILITIES AND NET ASSETS	
CURRENT LIABILITIES:	
Accounts payable	\$ 12,205
Accrued interest	49,391
Accrued salaries and related items	122,877
Current portion of long-term debt	30,000
TOTAL CURRENT LIABILITIES	214,473
NONCURRENT LIABILITIES:	
Noncurrent portion of long-term obligations	1,605,000
TOTAL LIABILITIES	1,819,473
NET ASSETS:	
Invested in capital assets, net of related debt	182,300
Restricted for debt service	208,172
Unrestricted	449,139
TOTAL NET ASSETS	839,611
TOTAL LIABILITIES AND NET ASSETS	\$ 2,659,084

**ISLAND CITY ACADEMY
STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2007**

<u>Functions/programs</u>	<u>Expenses</u>	<u>Program revenue</u>		<u>Governmental activities</u>
		<u>Charges for services</u>	<u>Operating grants</u>	<u>Net (expense) revenue and changes in net assets</u>
Governmental activities:				
Instruction	\$ 737,852	\$	\$	\$ (737,852)
Support services	369,510		37,296	(332,214)
Food services	25,482	11,250	11,132	(3,100)
Interest on long-term debt	118,719			(118,719)
Unallocated depreciation	53,711			(53,711)
Total governmental activities	<u>\$1,305,274</u>	<u>\$ 11,250</u>	<u>\$ 48,428</u>	<u>(1,245,596)</u>
General revenues:				
State of Michigan school aid unrestricted				1,427,053
Local sources				11,424
Contributed playground equipment				28,749
Investment revenue				15,617
Total general revenues				<u>1,482,843</u>
CHANGE IN NET ASSETS				237,247
NET ASSETS, beginning of year				<u>602,363</u>
NET ASSETS, end of year				<u>\$ 839,610</u>

**ISLAND CITY ACADEMY
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2007**

	General fund	Debt service	Nonmajor governmental funds	Total governmental funds
ASSETS				
ASSETS:				
Cash	\$ 267,498	\$	\$ 50,771	\$ 318,269
Investments		229,219		229,219
Receivables:				
Other governmental units	257,995			257,995
Due from other funds		28,344		28,344
Prepaid expenditures	36,301			36,301
TOTAL ASSETS	\$ 561,794	\$ 257,563	\$ 50,771	\$ 870,128
LIABILITIES AND FUND BALANCES				
LIABILITIES:				
Accounts payable	\$ 12,205	\$	\$	\$ 12,205
Accrued salaries and related items	122,877			122,877
Due to other funds	28,344			28,344
TOTAL LIABILITIES	163,426			163,426
	General fund	Debt service	Nonmajor governmental funds	Total governmental funds
FUND BALANCES:				
Reserved for prepaid expenditures	36,301			36,301
Reserved for debt service		257,563		257,563
Designated for future building and site expenditures			50,771	50,771
Designated for future expenditures	50,886			50,886
Undesignated	311,181			311,181
TOTAL FUND BALANCES	398,368	257,563	50,771	706,702
TOTAL LIABILITIES AND FUND BALANCES	\$ 561,794	\$ 257,563	\$ 50,771	\$ 870,128
Total governmental fund balances				\$ 706,702
Amounts reported for governmental activities in the statement of net assets are different because:				
Capital assets used in governmental activities are not financial resources and are not reported in the fund:				
The cost of the capital assets is		\$ 2,164,751		
Accumulated depreciation is		(347,451)		1,817,300
Long-term liabilities are not due and payable from current resources and are not reported in the fund:				
Certificates of participation				(1,635,000)
Accrued interest is not included as a liability in government funds, it is recorded when paid				(49,391)
Net assets of governmental activities				\$ 839,611

**ISLAND CITY ACADEMY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
YEAR ENDED JUNE 30, 2007**

	General fund	Debt service	Nonmajor governmental funds	Total governmental funds
REVENUES:				
Local sources	\$ 17,379	\$ 8,892	\$ 12,021	\$ 38,292
State sources	1,427,053			1,427,053
Federal sources	37,296		11,132	48,428
Total revenues	<u>1,481,728</u>	<u>8,892</u>	<u>23,153</u>	<u>1,513,773</u>
EXPENDITURES:				
Current:				
Instruction:				
Basic instruction	688,474			688,474
Added needs	49,378			49,378
Total instruction	<u>737,852</u>			<u>737,852</u>
Support services:				
Pupil	7,477			7,477
General administration	104,999			104,999
School administration	192,989			192,989
Business	10,200			10,200
Operations and maintenance	117,568			117,568
Total support services	<u>433,233</u>			<u>433,233</u>
Food service			25,482	25,482
Debt service:				
Principal retirement		30,000		30,000
Interest and fiscal charges		119,625		119,625
Total expenditures	<u>1,171,085</u>	<u>149,625</u>	<u>25,482</u>	<u>1,346,192</u>
EXCESS (DEFICIENCY) OF REVENUES UNDER (OVER) EXPENDITURES	<u>310,643</u>	<u>(140,733)</u>	<u>(2,329)</u>	<u>167,581</u>
OTHER FINANCING SOURCES (USES):				
Operating transfers in		141,883	53,100	194,983
Operating transfers out	(194,983)			(194,983)
Total other financing sources (uses)	<u>(194,983)</u>	<u>141,883</u>	<u>53,100</u>	
NET CHANGE IN FUND BALANCES	115,660	1,150	50,771	167,581
FUND BALANCES:				
Beginning of year	282,708	256,413		539,121
End of year	<u>\$ 398,368</u>	<u>\$ 257,563</u>	<u>\$ 50,771</u>	<u>\$ 706,702</u>

**ISLAND CITY ACADEMY
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2007**

Net change in fund balances total governmental funds	\$ 167,581
 Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. In the statement of activities, these costs are allocated over their estimated useful lives as depreciation.	
Depreciation expense	(53,711)
Capital outlay	92,472
 Non-cash contribution of playground equipment .	
Contribution revenue	28,749
Donated capital assets	(28,749)
 Accrued interest on certificates of participation is recorded in the statement of activities when incurred; it is not recorded in governmental funds until it is paid:	
Accrued interest payable, beginning of the year	50,297
Accrued interest payable, end of the year	(49,391)
 Proceeds and repayments of principal on long-term debt are other financing sources and expenditures in the governmental funds, but not in the statements of activities (where they are additions and reductions of liabilities)	
Principal repayment	30,000
 Change in net assets of governmental activities	 \$ 237,248

**ISLAND CITY ACADEMY
STATEMENT OF FIDUCIARY ASSETS AND LIABILITIES
JUNE 30, 2007**

ASSETS

	<u>Agency fund</u>
Cash	<u>\$ 1,517</u>

LIABILITIES

Due to student groups	\$ 399
Due to parent/teacher groups	<u>1,118</u>
	<u>\$ 1,517</u>

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the Island City Academy have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the Academy's accounting policies are described below.

A. Reporting Entity

Island City Academy (the "Academy") is a public school academy as part of the Michigan Public School System under Public Act No. 362 of 1993. Central Michigan University is the authorizing body for the Academy. The Academy's board of directors is approved by the authorizing body and is authorized to manage the Academy and the property and affairs of the Academy. The Academy receives funding from local, state, and federal government sources and must comply with all of the requirements of these funding source entities. However, the Academy is not included in any other governmental reporting entity as defined by accounting principles generally accepted in the United States of America. In addition, the Academy's reporting entity does not contain any component units as defined in Governmental Accounting Standards Board Statements No. 14 and No. 39.

B. Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the Academy. For the most part, the effect of interfund activity has been removed from these statements. The government-wide financial statements categorize primary activities as either governmental or business type. All of the Academy's activities are classified as governmental activities.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segments are offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges paid by recipients who purchase, use or directly benefit from goods or services by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. State Foundation Aid and other unrestricted items are not included as program revenues but instead as *general revenues*.

In the government-wide statement of net assets, the governmental activities column (a) is presented on a consolidated basis, and (b) is reported on a full accrual, economic resource basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations. The Academy's net assets are reported in three parts - invested in capital assets, net of related debt, restricted net assets; and unrestricted net assets.

The Academy first utilizes restricted resources to finance qualifying activities.

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Government-wide and Fund Financial Statements (Continued)

The government-wide statement of activities reports both the gross and net cost of each of the Academy's functions. The functions are also supported by general government revenues (state revenue, certain intergovernmental revenues, investment income and other revenue). The statement of activities reduces gross expenses by related program revenues and operating grants. Program revenues must be directly associated with the function. Operating grants include operating-specific (either operating or capital) grants.

The net costs (by function) are normally covered by general revenue (state sources, intergovernmental revenue, interest income and other revenues.)

The Academy does not allocate indirect costs.

This government-wide focus is more on the sustainability of the Academy as an entity and the change in the Academy's net assets resulting from the current year's activities.

Separate financial statements are provided for governmental funds and fiduciary funds, even though the latter are excluded from government-wide financial statements. Major individual governmental funds are reported as separate columns in the fund financial statements.

Governmental Funds - Governmental funds are those funds through which most Academy functions typically are financed. The acquisition, use and balances of the Academy's expendable financial resources and the related current liabilities are accounted for through governmental funds.

The Academy reports the following major governmental funds:

The *general fund* is the Academy's primary operating fund. It accounts for all financial resources of the Academy, except those required to be accounted for in another fund.

The *debt service fund* accounts for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

Other non-major funds

The *school lunch fund* accounts for activity related to the preparation and service of food to children of the school.

The *capital projects fund* accounts for the receipt of debt proceeds and the acquisition of fixed assets or construction of major capital projects.

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Government-wide and Fund Financial Statements (Concluded)

Fiduciary funds account for assets held by the Academy in a trustee capacity or as an agent on behalf of others. Trust funds account for assets held by the Academy under the terms of a formal trust agreement. Fiduciary funds are not included in the government-wide statements.

The *agency fund* is custodial in nature and does not present results of operations or have a measurement focus. Agency funds are accounted for using the accrual basis of accounting. This fund is used to account for assets that the Academy holds for others in an agency capacity (primarily student activities).

C. Measurement Focus, Basis of Accounting and Basis of Presentation

Accrual Method

The government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*, as are the fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

Modified Accrual Method

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Academy considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures as well as expenditures related to claims and judgments, are recorded only when payment is due.

State and federal aid and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the Academy.

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Measurement Focus, Basis of Accounting and Basis of Presentation (Concluded)

State Revenue

The State of Michigan utilizes a foundation grant approach which provides for a specific annual amount of revenue per pupil based on a statewide formula. The Foundation is funded from state and local sources. Revenues from state sources are primarily governed by the School Aid Act and the School Code of Michigan. The Michigan Department of Education administers the allocation of state funds to the Academy based on information supplied by the Academy. For the year ended June 30, 2007, the foundation allowance was based on pupil membership counts taken in February and September of 2006.

The state portion of the foundation is provided primarily by a state education property tax millage of 6 mills and an allocated portion of state sales and other taxes. The State revenue is recognized during the foundation period and is funded through payments from October 2006 to August 2007. Thus, the unpaid portion at June 30th is reported as due from other governmental units.

The Academy also receives revenue from the state to administer certain categorical education programs. State rules require that revenue earmarked for these programs be used for its specific purpose. Categorical funds received, which are not expended by the close of the fiscal year are recorded as deferred revenue.

D. Other Accounting Policies

1. Cash and equivalents include amounts in demand deposit accounts.

The Academy reports its investments in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools* and No. 40, *Deposits and Investment Risk Disclosures*. Under these standards, certain investments are valued at fair value as determined by quoted market prices, or by estimated fair values when quoted market prices are not available. The standards also provide that certain investments are valued at cost (or amortized cost) when they are of a short-term duration, the rate of return is fixed, and the Academy intends to hold the investment until maturity.

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Other Accounting Policies (Continued)

State statutes authorize the Academy to invest in bonds and other direct and certain indirect obligations of the U.S. Treasury; certificates of deposit, savings accounts, deposit accounts, or depository receipts of a bank, savings and loan association, or credit union, which is a member of the Federal Deposit Insurance Corporation, Federal Savings and Loan Insurance Corporation, or National Credit Union Administration, respectively; in commercial paper rated at the time of purchase within the three highest classifications established by not less than two standard rating services and which matures not more than 270 days after the date of purchase. The Academy is also authorized to invest in U.S. Government or federal agency obligation repurchase agreements, bankers' acceptances of U.S. banks, and mutual funds composed of investments as outlined above.

2. Prepaid expenditures

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid expenditures.

3. Receivables and payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the noncurrent portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

All receivables are shown net of an allowance for uncollectible amounts, if any.

4. Capital assets

Capital assets purchased or acquired are capitalized at historical cost or estimated historical cost. Donated fixed assets are valued at their estimated fair market value on the date received.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Improvements are capitalized and depreciated over the remaining useful lives of the related capital assets.

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Concluded)

D. Other Accounting Policies (Concluded)

Depreciation on all assets is provided on the straight-line basis over the estimated useful lives as follows:

Buildings and additions	50 years
Computer equipment	5 years
Furniture and other equipment	5 - 20 years

The Academy's capitalization policy is to capitalize individual amounts exceeding \$1,000.

5. Long-term obligations

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities on the statement of net assets. Certificates of participation premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight line method over the term of the related debt.

In the fund financial statements, governmental fund types recognize certificates of participation premiums and discounts, as well as bond issuance costs during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether of not withheld from the actual debt proceeds received, are reported as debt service expenditures.

6. Use of estimates

The process of preparing financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions regarding certain types of assets, liabilities, revenues, and expenditures. Such estimates primarily relate to unsettled transactions and events as of the date of the financial statements. Accordingly, upon settlement, actual results may differ from estimated amounts.

7. Fund balance

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 2 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America. Annual appropriated budgets are adopted for the general and special revenue funds. Encumbrance accounting is employed in governmental funds. Significant encumbrances outstanding at year end, if any, are reported as reservations of fund balance because they will be re-appropriated in the subsequent fiscal year.

The Academy follows these procedures in establishing the budgetary data reflected in the financial statements:

1. The School Administrator submits to the Board of Education a proposed operating budget for the fiscal year commencing on July 1. The operating budget includes proposed expenditures and the means of financing them. The level of control for the budgets is at the functional level as set forth and presented as required supplementary information.
2. Prior to July 1, the budget is legally adopted by Board of Education resolution pursuant to the Uniform Budgeting and Accounting Act (1968 PA 2). The Act requires that the budget be amended prior to the end of the fiscal year when necessary to adjust appropriations if it appears that revenues and other financing sources will be less than anticipated or so that expenditures will not be in excess of original estimates. Expenditures shall not be made or incurred, unless authorized in the budget, in excess of the amount appropriated. Violations, if any, in the general fund are noted in the required supplementary information section.
3. The School Administrator is authorized to transfer budgeted amounts between major expenditure functions within any fund; however, these transfers and any revisions that alter the total expenditures of any fund must be approved by the Board.
4. Formal budgetary integration is employed as a management control device during the year for the general fund.
5. The budget was amended during the year with supplemental appropriations, the last one approved prior to June 30, 2007.

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 3 - DEPOSITS, INVESTMENTS AND CREDIT RISK

As of June 30, 2007, the Academy had the following investments.

<u>Investment Type</u>	<u>Fair value</u>	<u>Weighted average maturity (years)</u>	<u>Standard & Poor's Rating</u>	<u>%</u>
First American Treasury Obligation Fund - class D	<u>\$ 229,219</u>	0.0027	AAA	<u>100%</u>
Portfolio weighted average maturity		<u>0.0027</u>		

1 day maturity equals 0.0027, one year equals 1.00

The Academy voluntarily invests certain excess funds in external pooled investment funds which included treasury obligations. The treasury obligation reports as of June 30, 2007, the fair value of the Academy's investments is the same as the value of the pool shares. The above investments are restricted for payment of debt service.

The Academy does not currently have an investment policy.

Interest rate risk. The Academy will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates, by; structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities in the open market; and, investing operating funds primarily in shorter-term securities, liquid asset funds, money market mutual funds, or similar investment pools and limiting the average maturity in accordance with the Academy's cash requirements.

Credit risk. State law limits investments in commercial paper and corporate bonds to a prime or better rating issued by nationally recognized statistical rating organizations (NRSROs).

Concentration of credit risk. The Academy will minimize concentration of credit risk, which is the risk of loss attributed to the magnitude of the Academy's investment in a single issuer, by diversifying the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimized.

Custodial credit risk - deposits. In the case of deposits, this is the risk that in the event of a bank failure, the Academy's deposits may not be returned to it. As of June 30, 2007, \$221,631 of the Academy's bank balance of \$321,631 was exposed to custodial credit risk because it was uninsured and uncollateralized.

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 3 - DEPOSITS, INVESTMENTS AND CREDIT RISK (Concluded)

Custodial credit risk - investments. For an investment, this is the risk that, in the event of the failure of the counterparty, the Academy will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party.

The Academy will minimize custodial credit risk, which is the risk of loss due to the failure of the security issuer or backer, by; limiting investments to the types of securities allowed by law; and pre-qualifying the financial institutions, broker/dealers, intermediaries and advisors with which the Academy will do business.

Foreign currency risk. The Academy is not authorized to invest in investments which have this type of risk.

NOTE 4 - RECEIVABLES

Amounts due from other governmental units is the July and August state aid payments due from the State of Michigan.

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 5 - CAPITAL ASSETS

A summary of changes in the Academy's capital assets follows:

	<u>July 1, 2006</u>	<u>Additions</u>	<u>Deletions</u>	<u>June 30, 2007</u>
Assets not being depreciated:				
Land	\$ 96,082	\$	\$	\$ 96,082
Capital assets, being depreciated:				
Building	1,739,212	2,926		1,742,138
Computer equipment		39,954		39,954
Land improvements		37,856		37,856
Furniture and fixtures	236,985	11,736		248,721
Subtotal	<u>1,976,197</u>	<u>92,472</u>		<u>2,068,669</u>
Accumulated depreciation:				
Building	186,152	34,857		221,009
Computer equipment		5,304		5,304
Land improvements		472		472
Furniture and fixtures	107,588	13,078		120,666
Total accumulated depreciation	<u>293,740</u>	<u>53,711</u>		<u>347,451</u>
Net capital assets being depreciated	<u>1,682,457</u>	<u>38,761</u>		<u>1,721,218</u>
Net capital assets	<u>\$ 1,778,539</u>	<u>\$ 38,761</u>	<u>\$</u>	<u>\$ 1,817,300</u>

Depreciation for the fiscal year ended June 30, 2007 amounted to \$53,711. The Academy determined that it was impractical to allocate depreciation to the various governmental activities as the assets serve multiple functions.

NOTE 6 - LONG-TERM DEBT

The Academy issued certificates of participation for the acquisition, construction and improvement of major capital facilities, as well as, the purchase of equipment. These certificates of participation are direct obligations and pledge the full faith and credit of the Academy. Long-term debt currently outstanding at June 30 is as follows:

August 1999 certificates of participation - due in annual installments of \$30,000 to \$140,000 through August 2029; interest at 7.25%. Secured by pledged state aid, first mortgage on the property security interest in specific equipment and debt service reserve fund.

\$ 1,635,000

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 6 - LONG-TERM DEBT (Concluded)

The annual requirements to amortize long-term debt outstanding as of June 30, 2007, including interest of \$1,715,894 are as follows:

Year ending June 30,	Principal	Interest	Total
2008	\$ 30,000	\$ 117,450	\$ 147,450
2009	30,000	115,275	145,275
2010	35,000	112,919	147,919
2011	35,000	110,381	145,381
2012	40,000	107,663	147,663
2013 - 2017	240,000	490,099	730,099
2018 - 2022	350,000	384,250	734,250
2023 - 2027	485,000	233,994	718,994
2028 - 2030	390,000	43,863	433,863
	<u>\$ 1,635,000</u>	<u>\$ 1,715,894</u>	<u>\$ 3,350,894</u>

An amount of \$257,563 is available in the debt service funds to service the debt.

The following is a summary of long-term debt transactions of the Academy for the year ended June 30, 2007:

Long-term debt, July 1, 2006	\$ 1,665,000
Deletions	<u>(30,000)</u>
Long-term debt, June 30, 2007	<u>\$ 1,635,000</u>

Interest expense (all funds) for the year ended June 30, 2007 was \$119,625.

**ISLAND CITY ACADEMY
NOTES TO FINANCIAL STATEMENTS**

NOTE 7 - INTERFUND RECEIVABLES AND PAYABLES

Individual fund due to and from other funds at June 30, 2007 are as follows:

Fund	Due from other funds	Due to other funds
General fund	\$	\$ 28,344
Debt service fund	28,344	
Total	\$ 28,344	\$ 28,344

Outstanding balances between funds represent July and August State Aid payments to be paid by the General Fund to the Debt Service Fund.

NOTE 8 - RISK MANAGEMENT

The Academy is exposed to various risk of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees and natural disasters. To minimize the risk, the Academy carries commercial insurance.

NOTE 9 - INTERFUND TRANSFERS

During 2007, \$141,883 was transferred from the general fund to the debt service fund to pay principal and interest due on the certificates of participation. In addition, \$3,100 was transferred from the general fund to the school lunch fund for costs associated with food service. Finally, \$50,000 was transferred to the newly created capital projects fund for future building and site uses.

REQUIRED SUPPLEMENTARY INFORMATION

**ISLAND CITY ACADEMY
REQUIRED SUPPLEMENTAL INFORMATION
BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
YEAR ENDED JUNE 30, 2007**

	Original budget	Final budget	Actual	Variance with final budget positive (negative)
REVENUES:				
Local sources	\$ 6,000	\$ 14,750	\$ 17,379	\$ 2,629
State sources	1,263,000	1,403,737	1,427,053	23,316
Federal sources	750	56,000	37,296	(18,704)
Total revenues	<u>1,269,750</u>	<u>1,474,487</u>	<u>1,481,728</u>	<u>7,241</u>
EXPENDITURES:				
Instruction:				
Basic programs	631,770	735,500	688,474	47,026
Added needs	72,100	50,950	49,378	1,572
Total instruction	<u>703,870</u>	<u>786,450</u>	<u>737,852</u>	<u>48,598</u>
Support services:				
Pupil	10,000	10,000	7,477	2,523
Library		15,380		15,380
General administration	105,260	134,500	104,999	29,501
School administration	171,400	191,850	192,989	(1,139)
Business	13,500	13,500	10,200	3,300
Operations and maintenance	103,550	133,150	117,568	15,582
Total support services	<u>403,710</u>	<u>498,380</u>	<u>433,233</u>	<u>65,147</u>
Total expenditures	<u>1,107,580</u>	<u>1,284,830</u>	<u>1,171,085</u>	<u>113,745</u>
EXCESS OF REVENUES OVER EXPENDITURES	162,170	189,657	310,643	120,986
OTHER FINANCING SOURCES (USES):				
Operating transfers out	(198,755)	(198,755)	(194,983)	3,772
NET CHANGE IN FUND BALANCE	<u>\$ (36,585)</u>	<u>\$ (9,098)</u>	115,660	<u>\$ 124,758</u>
FUND BALANCE:				
Beginning of year			<u>282,708</u>	
End of year			<u>\$ 398,368</u>	

ADDITIONAL INFORMATION

**ISLAND CITY ACADEMY ACADEMY
NONMAJOR GOVERNMENTAL FUND TYPES
COMBINING BALANCE SHEET
JUNE 30, 2007**

	Special revenue fund School lunch	Capital projects fund Building & site	Total nonmajor governmental funds
ASSETS			
ASSETS:			
Cash	\$	\$ 50,771	\$ 50,771
TOTAL ASSETS	\$	\$ 50,771	\$ 50,771
LIABILITIES AND FUND BALANCE			
FUND BALANCES:			
Designated for future building expenses and site expenditures	\$	\$ 50,771	\$ 50,771
TOTAL LIABILITIES AND FUND BALANCES	\$	\$ 50,771	\$ 50,771

**ISLAND CITY ACADEMY
NONMAJOR GOVERNMENTAL FUNDS
COMBINING STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
YEAR ENDED JUNE 30, 2007**

	Special revenue fund School Lunch	Capital projects fund Building & Site	Total nonmajor governmental funds
REVENUES:			
Local sources	\$ 11,250	\$ 771	\$ 12,021
Federal aid	11,132		11,132
Total revenues	<u>22,382</u>	<u>771</u>	<u>23,153</u>
EXPENDITURES:			
Food service	<u>25,482</u>		<u>25,482</u>
Total expenditures	<u>25,482</u>		<u>25,482</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(3,100)	771	(2,329)
OTHER FINANCING SOURCES:			
Operating transfer in	<u>3,100</u>	<u>50,000</u>	<u>53,100</u>
NET CHANGE IN FUND BALANCES		50,771	50,771
FUND BALANCES, beginning of year			
FUND BALANCES, end of year	<u>\$</u>	<u>\$ 50,771</u>	<u>\$ 50,771</u>



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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

To the Board of Education
Island City Academy
Eaton Rapids, Michigan

September 21, 2007

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Island City Academy as of and for the year ended June 30, 2007, which collectively comprise Island City Academy's basic financial statements and have issued our report thereon dated September 21, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Island City Academy's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Island City Academy's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Island City Academy's internal control over financial reporting.

Our consideration of the internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Academy's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Academy's financial statements that is more than inconsequential will not be prevented or detected by the Academy's internal control. We consider the deficiencies described as 2007-1 and 2007-2 in the accompanying schedule of findings and responses to be significant deficiencies in internal control over financial reporting.

To the Board of Education
Island City Academy
Eaton Rapids, Michigan

September 21, 2007

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Academy's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, the significant deficiency described above as 2007-1 we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Island City Academy's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of Island City Academy's in a separate letter dated September 21, 2007.

Island City Academy's response to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit Island City Academy's response and, accordingly, we express no opinion on it.

This report is intended for the information of the Board of Education, management and the Michigan Department of Education and is not intended to be and should not be used by anyone other than these specified parties.

Maner, Costrison & Ellis, P.C.

Certified Public Accountants

Schedule of Findings and Responses

Finding 2007-1

Finding considered a material weakness

Criteria:

The school's debt service fund is a major fund of the Academy and thus the activity needs to be reported in the annual financial statements. Also, during the year the Academy began a school lunch program. The Michigan Department of Education school accounting manual recommends lunch activity to be recorded in a special revenue fund.

Condition

The Academy has not recorded the activity of the fund. Material entries are made as part of the audit on an annual basis to record the activity of the debt service fund. The Academy recorded the school lunch program activity in the trust and agency fund.

Effect

Because material journal entries are made by the external auditors, a material weakness exists as defined by SAS #112.

Recommendation

Recording the activity of the funds on a monthly basis (via a spreadsheet program) would be sufficient documentation. Also, a separate bank account should be considered for the school lunch program.

Client Response

We are aware of these issues and will work with our accountant to establish a system of recording the activity of the debt service fund on a monthly basis. This should provide a summary for the annual financial statements. We have already established a separate bank account and reporting system for the school lunch program.

Schedule of Findings and Responses

Finding 2007-2

Finding considered a significant deficiency

Criteria:

Effective for the year ended June 30, 2007, Statement on Auditing Standards #112 titled *Communicating Internal Control Related Matters Identified in an Audit* (issued May 2006), requires communication in writing when an entity requires assistance to prepare the financial statements, including the footnotes, in accordance with accounting principles generally accepted in the United States of America.

Condition

Currently, the Academy's bookkeeper prepares the interim financial reports and assists the external auditor in the preparation of the annual financial statements.

Cause

The staff and bookkeeper of the Academy understand all the information included in the annual financial statements; however, assistance of the external auditor was utilized in preparing the footnotes to the financial statements and certain reconciliations required by Governmental Accounting Standards Board Statement #34.

Effect

Utilization of the external auditor in preparing the footnotes and certain reconciliations to the financial statements assists management with the external financial reporting responsibility. The current process meets the definition of a significant deficiency as defined in Statement on Auditing Standards #112.

Recommendation

At this time, no changes are recommended, this is only being communicated as required by professional standards.

Client Response

The Academy is aware of this deficiency and believes it is not cost beneficial to develop this expertise. The Academy will continue to use the external auditors for this technical assistance and would expect this situation to be ongoing.



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September 21, 2007

To the Board of Education
Island City Academy
Eaton Rapids, Michigan

In planning and performing our audit of the financial statements of Island City Academy as of and for the year ended June 30, 2007, in accordance with auditing standards generally accepted in the United States of America, we considered Island City Academy's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Academy's internal control. Accordingly, we do not express an opinion on the effectiveness of the Academy's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies and other deficiencies that we consider to be material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Academy's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Academy's financial statements that is more than inconsequential will not be prevented or detected by the Academy's internal control. We consider the following deficiencies to be significant deficiencies in internal control:

Assistance with Annual Financial Statements

Currently, the Academy's has hired an outside bookkeeper who prepares the interim and annual financial statements. Effective for the year ended June 30, 2007, Statement on Auditing Standards #112 titled *Communicating Internal Control Related Matters Identified in an Audit* (issued May 2006), requires us to communicate in writing when a client requires assistance to prepare the financial statements and footnotes in accordance with accounting principles generally accepted in the United States of America. The staff of the Academy does understand all information included in the annual financial statements; however, we assist in preparing the footnotes to the annual financial statements. We do not recommend any changes to this situation at this time and communicate this as required by professional standards. We believe this meets the definition of a significant deficiency as defined in Statement on Auditing Standard #112.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We believe that the following deficiencies constitute material weaknesses:

Debt Service Fund and School Lunch Fund

Currently, no one at the academy, nor the academy's bookkeeper, records the activity of the Academy's debt service fund. As a major fund of the Academy, the activity of the debt service fund must be summarized and recorded in the year-end financial statements. Due to the low level of activity that occurs in the debt fund, it may be more beneficial to record the activity using a spreadsheet program instead of the typical double entry accounting system. At a minimum, this summary should include totals for investments held, investment income, interest and principal payments, total of refunds to general fund, and an estimate of the amount due from general fund at year end. We believe this meets the definition of a material weakness within Statement of Auditing Standard #112.

It was also noted that during the year the Academy recorded the food service activity within the trust and agency fund. Food service activity is required to be recorded in a separate special revenue (school lunch) fund. The Academy should establish a separate school lunch fund to record the activity.

In addition, during our audit, we noted certain matters involving the internal control and other operational matters that are presented for your consideration. This letter does not affect our report dated September 21, 2007 on the financial statements of Island City Academy. We will review the status of these comments during our next audit engagement. Our comments and recommendations, all of which have been discussed with appropriate members of management, are intended to improve the internal control or result in other operating efficiencies. We will be pleased to discuss these comments in further detail at your convenience, perform any additional study of these matters, or assist you in implementing the recommendations. Our comments are summarized as follows:

Online Purchases

During the course of the audit, it was noted that the school recently acquired a debit card in part to facilitate supply purchases made via online stores. It was noted that on few occasions proper support was not readily available for these purchases. This was caused by invoices not being printed for all online purchases. To ensure all online purchases have proper support, staff should print a “screen print” of the check-out invoice when the transaction is being processed. This will ensure proper documentation is maintained when the online vendor does not provide an invoice with the shipped items.

Budget

It was noted during the course of the audit that a separate budget was not being prepared for the school’s debt service and school lunch funds. The Board should prepare a separate budget for each of the school’s funds. These budgets should also account for transfers made between funds.

New Notification Requirements for Related Not-for-Profit Organizations with Gross Receipts of \$25,000 or less Such as Booster Groups and PTO’s

The Pension Protection Act of 2006 requires these organizations to file an annual electronic notice for tax periods beginning after December 31, 2006, if these organizations are not required to file Form 990 (or 990-EZ), Return of Organization Exempt From Income Tax because their gross receipts are normally \$25,000 or less.

If they are a section 509(a)(3) supporting organization, generally, they must file a paper or electronic Form 990 (or Form 990-EZ) even if their gross receipts are normally \$25,000 or less. However, if they are a supporting organization of a religious organization and their gross receipts are normally \$5,000 or less they may file an annual electronic notice instead of Form 990 (or Form 990-EZ).

The annual electronic notice is due by the 15th day of the fifth month after the close of their tax period. For example, if their tax period ends on December 31, 2007, the annual electronic notice is due May 15, 2008.

The notice will require these organizations to provide the following information:

- Organization's legal name,
- Any other names your organization uses,
- Organization's mailing address,
- Organization's website address (if applicable),
- Organization's employer identification number (EIN),
- Name and address of a principal officer of your organization.
- Organization's annual tax period,
- Verify that your organization's annual gross receipts are still normally \$25,000 or less, and;
- Indicate if your organization has terminated (is no longer in business).

New Auditing Standards

Recently, 10 new auditing standards have been released and are effective, or will become effective for your June 30, 2008 year end. In reviewing the new standards, they will have an impact on our overall audit approach. The trend is to perform audit procedures utilizing more of a risk based approach. One area which will continue to be emphasized is your internal controls.

We have already discussed many of these comments and suggestions with various Academy personnel, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

To the Board of Education
Island City Academy
Eaton Rapids, Michigan

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September 21, 2007

This report is intended solely for the information and use of Island City Academy, management, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

We appreciate the cooperation we received from your staff during our engagement and the opportunity to be of service.

Very truly yours,

Maner, Costrison & Ellis, P.C.



Lamonte T. Lator
Bruce J. Dunn
Jeffrey C. Stevens
Linda I. Schirmer
Steven W. Scott
David M. Raeck
Robert E. Miller, Jr.
Steven B. Robbins
James E. Nyquist
James R. Dedyne

Timothy H. Adams
David B. Caldwell
Edward L. Williams, III
Timothy J. Orians
Dennis D. Theis

Walter P. Maner, Jr. (1921-2004)
Floyd L. Costerisan
Leon A. Ellis (1933-1988)

September 21, 2007

To the Board of Directors
Island City Academy
Eaton Rapids, Michigan

We have audited the financial statements of Island City Academy for the year ended June 30, 2007, and have issued our report thereon dated September 21, 2007. Professional standards require that we provide you with the following information related to our audit.

1. Our Responsibility under Auditing Standards Generally Accepted in the United States of America

As stated in our engagement letter our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance about whether the financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

As part of our audit, we considered the internal control of Island City Academy. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of Island City Academy's compliance with certain provisions of law, regulations, contracts and grants. However, the objective of our tests was not to provide an opinion on compliance with such provisions.

2. Significant Accounting Policies

Management has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by Island City Academy are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2007. We noted no transactions entered into by Island City Academy during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus. However, the Academy instituted a special revenue fund for the newly started school lunch program.

3. Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was for the depreciable lives of capital assets.

4. Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the school district's financial reporting process (that is, cause future financial statements to be materially misstated). In our judgment, the adjustments we proposed, related to the debt service fund, indicate matters that could have a significant effect on the school district's financial reporting process. Management has approved all adjustments.

5. Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

6. Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

7. Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Academy's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

To the Board of Directors
Island City Academy
Eaton Rapids, Michigan

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September 21, 2007

8. Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing our audit.

This information is intended solely for the use of the finance committee, board of directors, and management of Island City Academy and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

Maner, Costrison & Ellis, P.C.